

CALIFORNIA ECONOMIC STRATEGY PANEL

Manufacturing Value Chain Work Group

Summary
June 15, 2005

Panel Members

Jim Beno
Lou Anne Bynum
Barry Hibbard
Jerold Neuman
Joe Fernandez (Conference Call)

Technical Advisors and Others

Woody Clark
Bruce DeVine
Gene Eisenbeisz
Doug Henton
Ed Kawahara
Trish Kelly
Jack Keyser
Mark Pisano
Suzanne Trimbath
Goetz Wolff

Introduction

Mark Pisano, Executive Director of the Southern California Council of Governments (SCAG), welcomed the Work Group and provided observations about the Southern California Regional Economy.

- The economy is in transformation. The economy has not stabilized from the reduction in basic manufacturing over the past 15 years. The region is in need of a new strategy.
- The participation of the region as a global gateway is the Southern California Region's future. The competition is now "megapolitan" regions. There are eight to ten megapolitan regions in the U.S. They include New York, Charlotte-Atlanta-Norfolk (parts of eight states trying to be a financial center), Bay Area, Chicago and Southern California.

- The Southern California megapolitan region includes the area from Bakersfield, Las Vegas to San Diego, and includes Tijuana and Mexicali. The U.S. gateways are competing globally and the Southern California megapolitan region needs to improve and invest.
- A competitive global gateway requires efficient goods movements, value-added production and distribution, marketing and financing. The success of the gateway hinges on just-in-time (logistics) delivery and production of products, and requires infrastructure including all the ports.
- Los Angeles has several valued industries such as high tech and entertainment that should be mobilized but they do not define the Southern California Region's strategy. There are pieces of multiple sectors in place and there is an opportunity to recapture the Region's position through a global gateway strategy – as a logistics/manufacturing/trade center, with complementary strategies and attracting the capital to integrate the components. This approach would make logistics a single industry, working to retain high value added manufacturing, and rebuild infrastructure, providing for construction jobs and environmental remediation. SCAG is working with regional leaders on a regional strategy to build the necessary infrastructure. The theme of the overall strategy is “Recapturing the Dream.”

Ed Kawahara explained that the purpose of the Work Group is to review the analysis and research findings of the manufacturing value chain sector in the broader context of infrastructure. There are challenges for the regions in the global context that State government needs to address. The role of the Economic Strategy Panel is to identify the policy issues and make recommendations to the Governor and the Legislature. He introduced Doug Henton and Jack Keyser to frame issues for future growth and competitiveness of manufacturing in the state, generally, and in Southern California.

Framing the Issues Regarding the State's Manufacturing Value Chain and Infrastructure Challenges/Global Competition

Doug Henton, President of Collaborative Economics, Inc. presented preliminary findings and issues on the future of manufacturing as part of the California Regional Economies Project.

Industry Trends

- The Manufacturing Value Chain is more complex than manufacturing production alone – it includes a value chain of design, production and logistics activities linked to the customer. These components are integrated into global supply chains. Manufacturing production jobs are declining but productivity is increasing.

- The California Regional Economies Project is trying to organize activities in the logistics industry to address workforce and infrastructure demands. This industry includes: supply chain management (including inventory management and production planning), logistics support (i.e. warehousing and storage) and transportation services (i.e. the physical movement of goods).
- The logistics industry has evolved from a series of fragmented activities in the 1960s to total integration in the 1990s and holistic, integrated supply chain management, currently.
- Global competition requires sophisticated logistics networks. Reduced inventory and logistical costs create productivity gains. This requires the application of information technology tools.
- Over time the inventory to sales ratio has dropped in all manufacturing except semi-conductors, reflecting a major savings in logistics costs through just in time management of inventory, which has been due to information technology and has created a major productivity burst.

Employment Trends

- Logistics employment has increased in regions of California; however, average wage growth has been mixed.
- There are four major regions and corridors in California: Southern California, Bay Area, San Joaquin Valley and San Diego. All are growing except the Bay Area and the largest share is in Southern California, which experienced 22% employment growth from 1990 to 2003. The California Business, Transportation and Housing Agency has been assessing infrastructure needs to support goods movement strategies.
- Transportation services are being outsourced to couriers (UPS, Fed Ex, etc.) and employment far outpaces growth in transportation services. These third party firms provide a wide range of services which now includes assembly and repairs of some products.

Jack Keyser, Senior Vice President and Chief Economist of the Los Angeles County Economic Development Corporation discussed issues regarding manufacturing in the Southern California Region.

- There is no congestion at the Los Angeles and Long Beach ports currently. There is a need to add a port the size of Oakland every year in the U.S. to keep up with the current and projected pace of growth in trade.
- Business climate issues continue to be workforce and labor market (skills and ethics), workers comp, electric power rates and congestion. The manufacturing

sector is feeling beaten down. Manufacturing employment has declined in Los Angeles County and there has been modest growth in the region.

- There is low industrial vacancy rate of 1.2 to 2%, with competition for land to be converted to retail uses for sales tax revenues.
- While manufacturing production has moved offshore, design, marketing and logistics remain in the region. There are many smaller niche manufacturing firms in the region, using independent contractors and temporary workers. Segments of major non-farm employment (truckers, professional services, smaller manufacturing) are at an all-time high.
- The economic base of the Southern California Region is tourism, international trade, technology-led industries, higher education and Indian gaming.
- Through a survey of manufacturing firms, the Los Angeles County Economic Development Corporation found that firms are investing in plants and equipment but not hiring.
- The Los Angeles County Economic Development Corporation is placing a priority focus on transportation congestion. The Corporation has organized the Southern California Leadership Council to look at the region as an integrated system (includes Bakersfield) and every industry sector within the region. There is collaboration with service providers and government entities.
- Some offshore manufacturing firms have expressed concern about quality control and time to market and may consider re-locating back to the U.S.

Summary of the Discussion

There was extensive discussion regarding the two presentations. The following provides highlights of the discussion organized by manufacturing and port issues and workforce and innovation issues.

Manufacturing and Port Issues

- Major investments are not being made in the manufacturing base. China is the major manufacturer, but recently there has been industrial strife.
- New York is upgrading its port infrastructure. New York has access to larger purchasing power than the Southern California Region.
- How to handle the influx of products in and out of the ports – the Long Beach and Los Angeles Ports are going to 24-hour operations, but it is not a solution. Ships are doubling in size, taking a week to unload. Need to get containers off the

docks and to distribution points – the ports are not equipped to handle this volume. The process is fairly labor intensive but moving more to automation.

- There are still 480,000 manufacturing jobs in the region. The question is what kind of manufacturing jobs are these?
- There has been some modest manufacturing growth in the Inland Empire. These are firms with 10-20 employees that fill niche markets and provide highly technical skills in areas that include exotic metals, plastics and composites.
- The Southern California experience has been different from the Bay Area Region, which has had R&D and technology transfer. What this leaves behind is very important. The Southern California Region has been hurt by the defense downturn, which did not leave the same kind of (private) R&D infrastructure behind.
- The U.S. does not take advantage of water transportation, as they do in Europe (i.e., high speed ferry boats). Who would pay for this? Get creative on financing (look at the Milken Institute paper on the Hydrogen Highway as a model).
- The private sector is shifting costs back to the public sector for transportation.

Workforce and Innovation Issues

- Workforce education is the greatest area to add value – firms always mention this. There is a shortage of qualified workers for the construction industry as well as for manufacturers and exporters.
- There is a shortage of workers at the low and high ends, including replacement workers. Those entering training programs for machinists and mechanics do not have the basic skills to enter the trades. Reading and computer skills are a requisite.
- The education system needs to be two tracks for college and career technical opportunities. The community colleges are dropping the industrial arts when there is a need for these skills.
- A recent study of 18-24 year olds in Long Beach found that 60% were not in any kind of education/training program.
- What is the manufacturing value chain morphing into and how does one anticipate and get information to the local level? There is a need for “real time information” for a real time economy for the state’s education and training system. The community colleges could respond but mandates from the State change. A level of commitment and flexibility is needed in order to respond. School districts and employers need to reach out to students on career pathway opportunities.

- Talk to companies on the ground to get a better sense of occupational and skill-set needs, especially across industries.
- Focus on innovation and quality – example provided of an East Los Angeles firm that makes terrazzo tile and successfully competes in China, due to high quality design, materials, speed and quality of labor.
- Customer-driven design adds value. All parts of the value chain have to have high quality and to work together to compete.

Preliminary Recommendations

Through the course of the discussion, a variety of recommendations were made to take back to the full CA Economic Strategy Panel and/or actions to be taken by the Panel. The preliminary recommendations include the following.

- The Panel can communicate new research findings, providing a common framework for developing State economic policy. The Panel can lead the discussion and drive the information to local and regional levels.
- The manufacturing sector is changing. While there is a loss of production jobs, as part of a larger system, logistics and design jobs are growing. It is a more complex system. The Panel can explain this transformation and identify growth areas. Some of these areas provide higher skill and higher wage jobs.
- The Panel can meet with manufacturers, especially from design and logistics firms to identify their opportunities and constraints five years out. Profile firms that are successfully competing overseas and understand success factors and recommend policies that support competitiveness. The Los Angeles County Economic Development Corporation is willing to organize focus groups representing the Southern California Region.
- Do not give up on the manufacturing sector. The Panel can re-evaluate cost and competitiveness factors, understand supply-chain dynamics better and develop a plan and policies to bring back firms that have left. The Panel can bring it forward to statewide attention. As an example, in the apparel industry there are factors in addition to production costs that may diminish the cost disadvantages for Southern California – including quality, logistics, time (e.g., customer taste and expectations change). Taste and design are an integral part of the product. It's still an open question about what makes sense to go off-shore.
- The Panel can better understand the logistics sector and develop supportive policies.

- The Panel can provide a framework to help communities and regions understand the real time needs of the economy.
- The Panel can work with community colleges and districts to make specific recommendations for how the Community College system can be responsive to real time needs to workforce training.

Next Steps

The Work Group agreed to focus on the design and logistics sectors, including infrastructure demands, by meeting with employers and industry representatives. The discussions will address growth and competitiveness issues and opportunities and constraints five years out. The Work Group will coordinate efforts with the Los Angeles County Economic Development Corporation and the Southern California Association of Governments.